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Council of the District of Columbia

PUBLIC OVERSIGHT HEARING ON THE DISTRICT OF COLUMBIA'S PROPERTY TAX ASSESSMENT
PROCESS AND PROPERTY TAX RATES

Testimony of Herbert J. Huff, Deputy Chief Financial Officer, Office of Tax and Revenue, before the Committee on Finance and Revenue

Good afternoon, Chairman Evans and members of the committee. I am Herbert Huff, Deputy Chief Financial Officer for the Office of Tax and Revenue (OTR). I am here today to provide testimony on the District of Columbia's real property assessments and tax rates for fiscal year 2003. With me today are Dr. William Henry Riley, certified appraisal evaluator (CAE) and director of the Real Property Tax Administration, and Mr. Thomas W. Branham, the District's chief assessor.

Introduction

Five years ago, the Office of Tax and Revenue began a comprehensive reformation of the real property tax administration. These efforts resulted in major improvements to land records management, real property assessment and appeal processes, and the administration of real property tax and tax relief programs. The efforts also included the hiring of experienced managers and staff trained in real property valuation and tax administration.

Today, the improved state of the District's assessment process has been confirmed by two independent experts who performed analyses of OTR's 2003 revaluation. These studies show that while there is room for improvement, OTR has adopted an "appropriately aggressive but responsible approach to tracking market changes in tri-groups 1 and 2." Later in my testimony I will share a few highlights from the findings and recommendations of these important studies, copies of which have been provided to each member of the Council and are available to the public on the Internet.

Law changes and the installation of a new integrated computer system have further improved the operations of the real property tax administration, making our processes comparable to neighboring jurisdictions and superior to that of many states. We have moved from a largely paper and pencil environment to a robust integrated tax system with extensive Internet capability that provides public access to more real estate data than ever before. In fact, the District's real property site now far exceeds what is provided online by any of the surrounding municipalities.

OTR has other initiatives underway that will allow us to improve and to continue to enhance real property assessment and tax administration, developing them over time with consistent management, resources and systems evolution.

Oversight Issues

Mr. Chairman, today's oversight hearing is a welcome opportunity to provide your committee and the Council with a comprehensive discussion of the assessment process, methods, and techniques used to value real estate in the most recent FY 2003 revaluation in the District of Columbia. Understandably, there are questions among our citizens regarding the assessment process, methodologies used and accuracy of appraisals, as well as concerns about the potential increase in property taxes. Real property assessment is complex, and the mechanics of the process are often difficult to convey. In the District of Columbia, this complexity is compounded by two major events occurring simultaneously: a rapidly escalating real estate market and the return to annual assessments from a period when the District statute mandated a triennial assessment. Both of these changes require us to perform some catch-up in the assessment of real estate after several years of relatively static values. OTR has concluded, and the two expert reports that examined the District assessment process agree, that the assessment system in place will accommodate the transition to an annual assessment program and property-specific appraisals.

Like the practice of medicine, the assessment process is not an exact science. Real estate markets are not perfect, and there is no such thing as a “model” assessment. But there is an acceptable range of value. Our most recent revaluation, methods, techniques and practices have met or surpassed the standards of the International Association of Assessing Officers (IAAO) and the requirements of Standard 6 of the Uniform Standards of Professional Appraisal Practice. All of these advancements help ensure that, generally, real property in the District of Columbia is fairly assessed and that taxes are efficiently and properly accounted and collected. In upholding the integrity and impartiality of his office, the assessor is not concerned with the generation of revenue, but only the fair and equitable valuation of property, as required by law.

The Assessment Process

In general, a property's assessment is an estimate of its market value. Market value is how much a property would sell for under normal conditions. In the District, property owners are notified on or before March 1 of the reassessment to be used for their upcoming fiscal year tax bill. District of Columbia law requires that real property be assessed at 100 percent of its estimated market value as of January 1 before the new tax year. After a property's total value is determined, the appropriate deductions and credits are applied for billing purposes.

Assessment Approaches

Four years ago, District law established a triennial assessment process. Triennial assessments required the city to be divided into three approximately equal and geographically contiguous groups of real property, and assessments were to be performed for each one-third of the city's real estate each year.

With the migration to several new computer software applications, OTR began using a market modeling technique that allows updating of real property values. We converted all real property data to a new relational database computer-assisted mass appraisal system, commonly known as CAMA, providing one repository for all District property information. CAMA speeds many of the manual calculation processes in real property valuation while allowing for uniform application of economic data, valuation model calibration, and extensive and timely performance analysis. The methods and techniques incorporated in the current system are a market calibrated cost approach, sales comparison approach, and an income approach to value.

In any CAMA system conversion, data and property edits must be completed to ensure accurate results. The CAMA system will be continuously re-calibrated to improve and maintain accuracy and uniformity in assessment.

A property-specific valuation was conducted in 1998 and 1999 for most properties using the old CAMA system. This year OTR converted to a new CAMA system and returned to the property specific valuation in four neighborhoods. The new CAMA system represents the latest technology available to assessment administrations. Remaining neighborhoods were valued using a market oriented trend analysis by reviewing real property sales, completing an analysis of the sales data, and developing market trend factors by unique neighborhood and sub-neighborhood. Mass appraisal standards provide that market trend updating of values is acceptable but should not be done for an extended period of time.

As we approach fiscal year 2003, two-thirds of the city's 170,000 properties have been assessed. In this transition back to annual assessments, the market has shown appreciation of 1 to 1.6 percent per month for single-family residences and condominiums. These increases are similar to surrounding jurisdictions, though Washington, D.C. has experienced the highest appreciation. In addition, next year OTR plans to physically inspect approximately 35,000 parcels, with particular attention to properties that have recently been sold or renovated.

Going forward, the capabilities of the CAMA system will allow OTR to improve accuracy in the FY 2004 valuation, thereby reducing reliance on trending as a means of valuing residential properties. The ongoing valuations using CAMA techniques will continue to improve assessment equity among individual properties.

It is also relevant to note that the District statute continues to prescribe the lowest residential tax rate for occupied property in the Washington metro area - 96 cents per \$100 of assessed value. In addition, District homeowners will benefit in upcoming tax years from the 25 percent property tax cap recently enacted by the Council.

Independent Reviews: FY 2003 Assessments

OTR conducts routine performance analysis on its methodology. Most recently, the Chief Financial Officer sought an independent review of the FY 2003 revaluation. Two nationally and internationally recognized experts in the field of real property assessment administration conducted this review. I would like to share with you a synopsis of the findings in these two reports that evaluated District assessment process and systems.

Review by Otho C.W. Fraher, CAE

Otho C.W. Fraher, CAE, conducted an on-site review of the methods, techniques, and practices used in the FY 2003 assessment in the District. He reviewed steps taken by OTR to improve the valuation and assessment process, the changes in the appeal process, and the approaches in the FY 2003 revaluation. Fraher, an expert in real property appraisal and assessment administration, is past president of the International Association of Assessing Officers. As former head of the Real Property Division of the Virginia Department of Taxation, he had oversight responsibility for assessment administration in all political subdivisions of the State of Virginia. Fraher's report found the "methodology used by the District in the past two years was appropriate for the circumstances. In addition several initiatives have been undertaken which will improve the process in future years. I make several recommendations which if implemented will further improve the system."

The reviewer further found that, "The methods, techniques, and practices of the District of Columbia Office of Tax and Revenue in the area of assessment administration are comparable to other jurisdictions, as well as, the appropriate IAAO standards." Finally, Fraher noted that OTR has a good, informal appeal process in place, and that assessment roll and real property data are on the Internet allowing property owners to make informed judgments on the accuracy of their assessments.

Review by Robert J. Gloudemans

Robert Gloudemans, of the firm of Almy, Gloudemans, Jacobs, and Denne, is an international expert in mass appraisal and assessment administration performance analysis and former administrator for the Arizona Department of Revenue, Division of Property Valuation and Equalization. Gloudemans conducted an on-site review of OTR's systems, methods, techniques, and practices, as well as an extensive performance analysis of the FY 2003 revaluation. His findings "conclude that the Office of Tax and Revenue achieved an appropriate and acceptable level of assessment in the areas reappraised (areas 1 and 2) and that equity among taxpayers in these areas was substantially improved and also meets industry standards." Gloudemans analyzed the reappraisal performance by property type, by grade of construction, by size of property, by age of property, and by neighborhood for single-family and condominium properties and concluded that there was particularly good equity of valuation in each of the categories.

Gloudemans conducted an analysis of unsold properties using multiple regression analysis that "strongly indicates that appraisal uniformity is considerably better for individual properties, sold and unsold, than traditional analyses would suggest." He indicates "that current assessments are well within IAAO standards..." and that "while there is certainly room for improvement, the current values are certainly very acceptable."

Accuracy of Assessments

District of Columbia assessors use all available vehicles to assure accuracy and uniformity of values among all property types. One of those performance measures is to compare the city assessment against the sales prices of homes of like properties in the immediate area. However, in a market as volatile as Washington, D.C., disparities can and do occur. We routinely control for unusually high or low home sales by eliminating such 'outlier' properties from trend analyses for the purposes of an area's assessment. Overall, however, OTR's assessment-to-sale results have been found to have a high

degree of accuracy and are in line with other similarly situated jurisdictions, and may, in fact, be better than expected in light of the area's unusually high real estate activity.

Property owners who disagree with their assessment may always appeal the decision. The first step is an informal first-level hearing at OTR, which generally consists of a discussion with an assessor. If the taxpayer is not satisfied with that result, he may proceed to the Board of Real Property Assessment and Appeals. The final step is to appeal the assessment to the District of Columbia Superior Court.

I believe it is testament to OTR's successful assessment program and outreach efforts that the rate of appeals this year has, in fact, been lower than last year. For the FY 2003 assessment cycle OTR valued more than 114,000 parcels of real estate for tax purposes. Of those, only 6,180 first level real property assessment appeals were filed, representing 5.42 percent of total assessment notices mailed. This percentage is on par with similar, surrounding jurisdictions. It is also less than the rate of appeals last year, which was 3,725 appeals per 56,000 appraisals, or a rate of 6.65 percent of total assessments.

Some have suggested that recent sales should dictate the assessment for the property sold. They suggest we use a system that, when a property sells for \$1 million the preceding year, the assessment for that particular property automatically be raised to \$1 million as the best evidence of fair market value. Unfortunately, the proposal raises but does not resolve the question of what to do about the assessment of surrounding properties. Should OTR consider the sale price of one home the default assessed value for the entire block? For OTR, this approach would raise serious constitutional issues.

The Supreme Court has interpreted the U.S. Constitution's equalization requirement by stating that "the constitutional requirement is the seasonable attainment of a **rough equality in tax treatment of similarly situated property owners**" [*Allegheny Pittsburgh Coal Co. v. County Commissioner of Webster County, West Virginia*, 488 U.S. 336, 343 (1988)]. This is the framework within which OTR must operate its real property assessment system. The District Code does not require physical inspection of every parcel of property each year. The District Court of Appeals has sanctioned the use of trending based upon assessment sales/ratio [*District of Columbia v. Green*, 310 A.2d 848, 856 (D.C. App. 1973)]. Thus, if OTR were to require that a particular sale be used as the default value for same or similar homes in the neighborhood or sub-neighborhood, OTR would run afoul of the Constitution.

Addressing Concerns

OTR proactively sought to address taxpayer concerns at the front end of the annual assessment program through a rigorous public education campaign. This effort started nearly two years ago – well before the first new assessment notice was mailed – and included numerous presentations at Advisory Neighborhood Commission and civic group meetings. Educational efforts also included the production and dissemination of brochures and other literature, media advisories and other outreach initiatives. Still, like any tax administration, OTR draws its share of detractors. As guardian of District revenue, we are inevitably required to take certain actions that may be unpopular or misunderstood by some taxpayers. Like any tax administration, the Office of Tax and Revenue inevitably has those who question initiatives and some that misunderstand our processes. Real property assessment is a complex area that elicits citizen concerns, particularly as real estate markets escalate and drive up appraisals. I would like to take a moment to address a few concerns that have recently been raised to the Council and clarify those corresponding points of law that govern OTR procedures.

First, OTR's FY 2003 assessment was conducted in accordance with all District statutory and constitutional requirements, and overall results have been found to be acceptable and valid.

Next, in regard to assessment notice requirements, the Fiscal Year 2002 Budget Support Act of 2001 repealed a requirement that the notice separately state the value of the land and the value of the improvement. It also repealed the requirement to provide a written reason for changing the assessed value. The first modification is consistent with case law that requires the property as a whole to be valued and not merely its separate components. The second modification was required by administrative necessity. OTR does not have the resources to specifically describe why each property's assessment increased or decreased.

Next, there was an assertion that all assessments must be within 5 percent of the property's estimated market value. There is no such requirement in the D.C. Official Code or municipal regulations. The only mention of 5 percent assessments pertains to appeals before the Board of Real Property Assessments and Appeals. A plain reading of that provision is that the board has no authority to change an assessment where their estimate of value deviates less than 5 percent from the assessment.

Finally, OTR was criticized for using a trend analysis to arrive at the FY 2002 and FY 2003 assessments. Trending based upon sales of similar properties is permitted by the D.C. Official Code and is considered an acceptable appraisal method under industry standards. This method is merely a market adjustment factor, and, as a form of application of the sales comparison approach to value, it is an acceptable method of assessing.

Conclusion

While the assessment process is not an exact science, there are acceptable ranges of value. The District of Columbia has consistently met industry valuation standards, and we continue to strive to further improve the process. We will increase our volume of physical inspections of individual properties, and we will link real property building permits, property pictures, multiple list information, and building sketches to our records as we audit property records. We will continue to place more information on the Internet, providing easy access to homeowners and other users of real property assessment information.

It is the Council's and Mayor's authority and discretion to determine tax policy and tax rates and bases. Once such determinations have been made, it is OTR's responsibility to fairly and equitably administer tax law as designated by the legislature. This is the intent and goal of all OTR operations, and particularly of the real property assessment administration.

I would like to thank the Chairman and the members of the committee for their support as we work to build truly 21st century tax administration for the District of Columbia. Thank you for this opportunity to testify. I would be pleased to answer any questions that you or the other members may have.